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American Can's Big Shakeout
What's Ahead for House Prices

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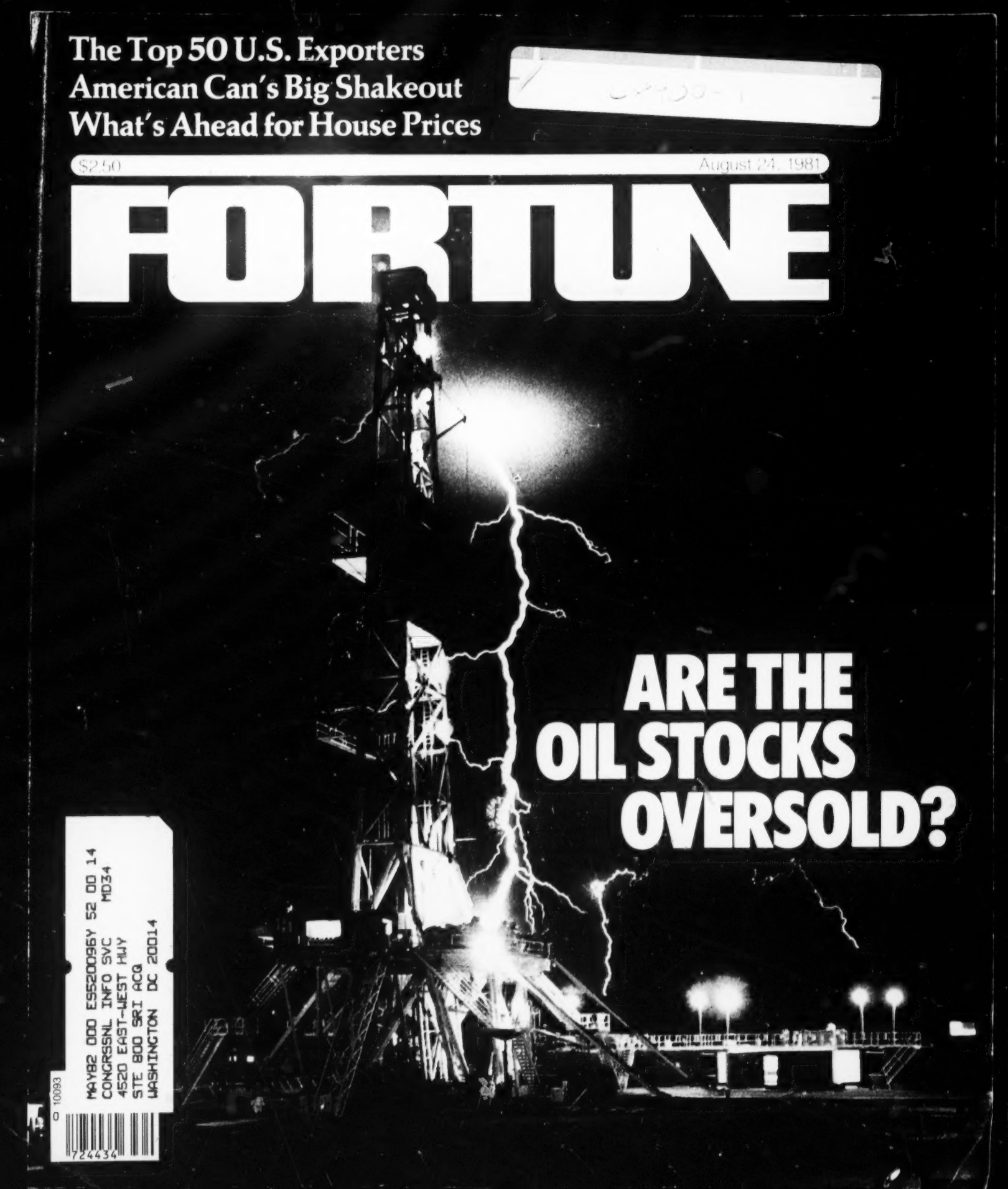

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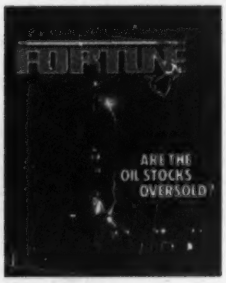

In Steve Krongard's cover photograph, lightning flashes around a Phillips Petroleum drilling rig in Arizona. A story on the outlook for big oil's storm-tossed stocks begins on page 50.

60 Liberals

74 American Can

84 Exporters

Departments

4 THE EDITOR'S DESK

7 IN THE NEWS
Houston Industries cuts its customers' voltage, Washington's deciding role in the battle for **Conoco**, **Heileman**'s plans to swallow **Schlitz**, a few drops of black ink at **Chrysler**, bad times at **MCA**, **Penn Central**'s deal with **Colt**—and more

21 LETTERS TO FORTUNE

41 FORTUNE FORECAST
Will high interest rates bring on a new recession?
Favorable omens from inventory plans: a survey

44 A DIFFERENCE OF OPINION
Paul Craig Roberts, an Assistant Secretary of the Treasury, tells why the tax cut will help savings

ACKNOWLEDGMENTS

16—Courtesy Penn Central, courtesy Colt Industry. 21—Nicholas Solovioff. 41,42—Chartmakers Inc. 47,48—Michael McGinn. 52—Daniel Kramer, George Palmisano, Daniel Kramer. 53—Régis Bossu/Sygma. 57—William Reduto. 60—Dennis Brack–Black Star. 61—Walter Bennett, Neil Leifer, Dirck Halstead. 62—Diana H. Walker, Anderson–Black Star, David Hume Kennerly. 63—Doug Bruce–Camera Five, Arthur Grace. 88—Inset courtesy Local 15, UAW. 113,116—Chart: Patricia Byrne, photography: Al Freni. 119—Graham Finlayson.

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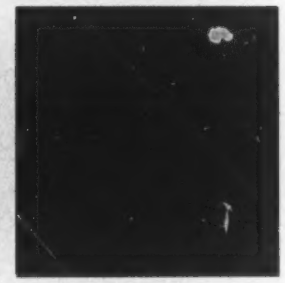
August 24, 1981

88 Unions



94 Lawn Tennis

47 KEEPING UP
by Daniel Seligman

109 BED AND BOARD
Reveille for a sleeper among Washington's hotels
by Jeremy Main

113 PERSONAL INVESTING
Why apparel stocks are in style
by Aimée L. Morner

119 BOOKS AND IDEAS
Talking back to the Third World
by William Bowen

INVESTMENTS
50 Are the Oil Stocks Oversold? *by Alexander Stuart*
They do look cheap, but a rebound is likely to hinge on exploration costs, demand, and the news from Saudi Arabia and Washington.

REAL ESTATE
57 It May Be Time to Rent *by A. F. Ehrbar*
In 18 months real house values may have declined by 8%. Under President Reagan, they could go on going down for years.

POLITICS
60 The Search for a Liberal Agenda *by Daniel Seligman*
In their time of trouble, liberals are sounding eerily like Jimmy Carter.

MERGERS
70 Don't Stop the Mating Game *by Walter Kiechel III*
Critics of the consolidation wave haven't made a convincing case.

TURNING POINTS
74 American Can's Big Shakeout *by Peter Nulty*
Unable to feed two capital-hungry businesses, the old tin-bender wants to stick with cans and cash in trees.

DIRECTORY
84 The Top 50 U.S. Exporters
Boeing is again No. 1, followed by GM, GE, and Ford.

WORKING SMARTER
88 What's in It for the Unions *by Charles G. Burck*
More cooperation with management could help stem their decline. (Last of a series)

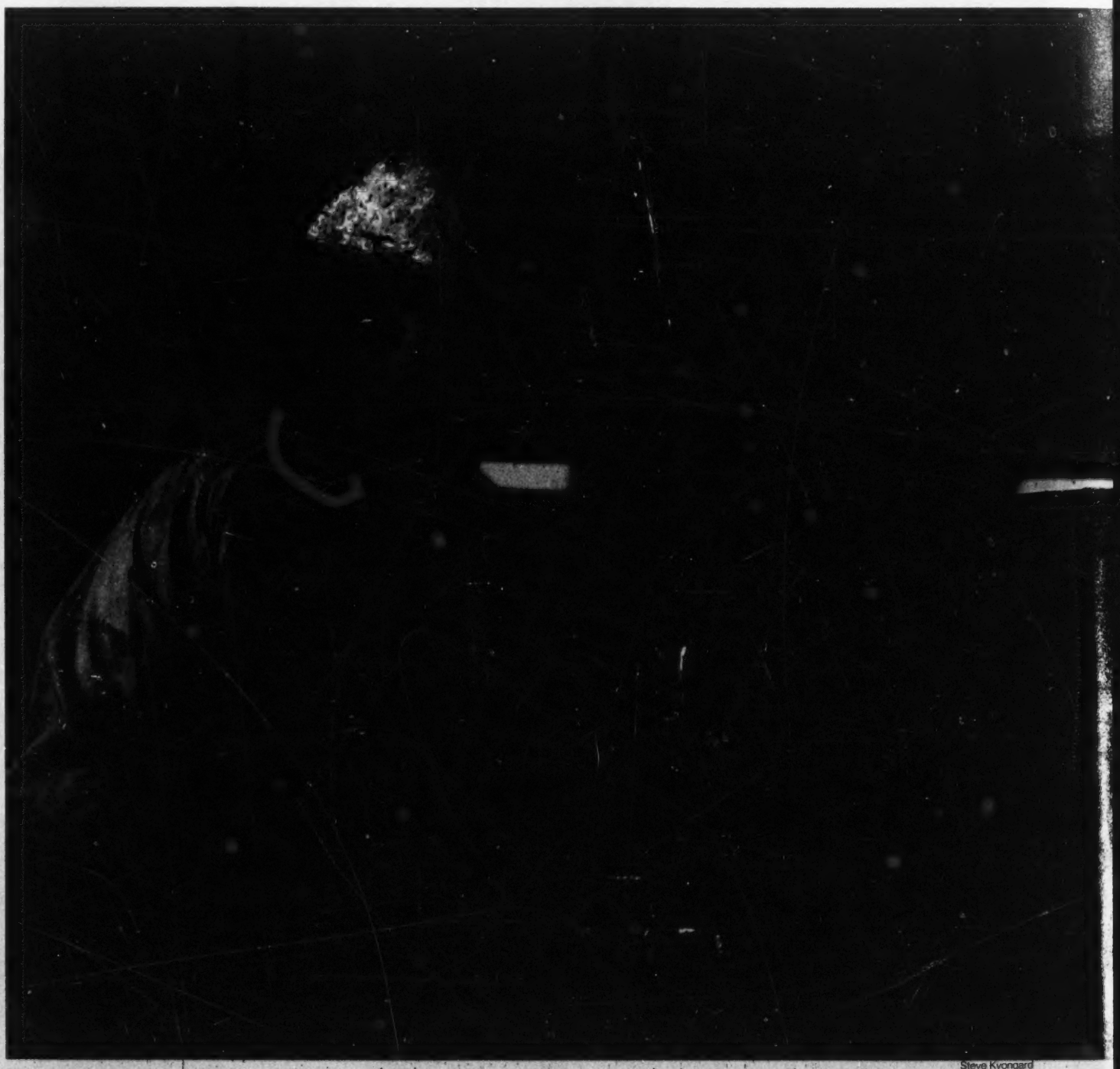
PICTURE PORTFOLIO
94 The Coolest Clubs in Tennis
The game on the greensward is exacting and elegant.

BANKING
102 A Two-Headed Bank Nibbles at the U.S. *by Robert Ball*
The disparate duo at the top of West Germany's Deutsche Bank hunger for a bigger American stake.

The U.S. Pushovers Push Back *by Edward Meadows*

INVESTMENTS

Are the Oil



Steve Kvongard

FORTUNE
August 24, 1981

Stocks Oversold?

by ALEXANDER STUART

From their peak last November, oil-company stocks have dropped with the glide slope of a stone. "It's one of the most massive and startling reversals of market leadership in modern times," one security analyst observes. Adds William F. Kieschnick, Atlantic Richfield's president and chief operating officer: "Energy stocks were 'in' last year and could do little wrong. Now they can do little right—unless a company is about to be acquired."

The share prices of the large integrated oil firms have declined 30% or more in some cases, though the recent clutch of merger bids—both rumored and real—has lifted the stocks of companies like Conoco, Marathon, and Cities Service since late June. Analysts can point to a raft of reasons to stay bearish about the group—a worldwide oil glut, slumping demand, falling crude prices. So the chief executive of a big integrated oil company may be forgiven for sounding a tad defensive when asked to explain Wall Street's disenchantment. "What sort of obituary notice are you going to write?" John E. Swearingen, chairman of Standard Oil Co. (Indiana), asked a recent visitor.

Big oil is hardly dying, however; it has merely lost its gravity-defying Superman qualities and rejoined the world of ordinary mortals. Earnings of U.S.-based integrated companies, propelled by a 150% jump in world oil prices, more than doubled over the two astounding years of 1979 and 1980. (Integrated companies' operations take in the full spectrum from finding and lifting to marketing.) The industry may have to settle for flat 1981 earnings or, at best, no more than a 5% rise.

With all that, big oil still deserves more envy than pity. The Value Line investment service projects the industry's return on equity for 1981 at 18.5%, down from a heady 23% in 1979 but still comfortably above the 14.4% achieved last year by the FORTUNE 500. Starting in 1982, moreover, earnings may begin to grow at a more respectable rate, though hardly at the otherworldly tempo of yesteryear. "I have a lot of trouble getting depressed about the oils," says Thomas A. Petrie, a veteran analyst with First Boston Corp.

> They do look cheap, but a rebound may hinge on changes in the cost of finding oil and in demand, and on the news from Saudi Arabia and Washington.

The oil stocks' fall was probably inevitable. They were overdue for a correction following what Barry C. Good, Morgan Stanley's top oil analyst, calls "the long bull march" that ended last fall. In 1980 energy stocks, including those of the oil-service firms, soared about 65%, far outpacing the 12% gain in the rest of Standard & Poor's 400-stock index. At times the bulls behaved like beasts in heat, pawing at the shares of the majors and independent producers with indiscriminate passion. "Investors saw one group with no problems and overbid it," says Edward J. Haase, a vice president of Chase Investors Management Corp., which runs a $7-billion investment portfolio.

Now the industry is perceived as awash in problems, including two quarters of profits that have been anything but obscene. In the first three months of 1981 the aggregate net income of 17 U.S.-based oil companies fell about 15% below last year's record level. The downward trend continued through the whole first half of 1981 for most majors, and some of the biggest of the big oils posted the sharpest declines: Gulf, off 19%; Indiana Standard, off 13%; Atlantic Richfield, off 16%. Amerada Hess, which earned $540 million in 1980 on sales of $7.9 billion, reported a $54-million loss in the second quarter—the first quarterly loss suffered by a major in years.

As these figures suggest, the decontrol of U.S. crude prices has been no bonanza. Shortly after President Reagan lifted controls in late January, the average price of U.S. crude jumped from $25.80 a barrel to about $36. This brightened the picture in the upstream end of the business—exploration and production—despite the heavy bite taken by the windfall-profits tax. Indiana Standard's net income from upstream operations, for example, jumped 67% in the first half.

But these gains were swamped by sharp profit declines in the industry's downstream segment—refining and marketing. When the effects of decontrol hit the pumps, consumers struck back. By the end of the first quarter, gasoline consumption was running 10% below the year-earlier level. Demand also slumped for other petroleum products, such as residual fuel oils. The upshot was that refineries burbled along at 70% of capacity or less in some weeks, way below profitable levels. The industry has responded to these dismal operating rates by mothballing roughly 600,000 to 700,000 barrels a day of refining capacity in the U.S. alone.

The cuts came too late to prevent red ink at Hess, which has to purchase about 80% of its crude supply, or Gulf, which is painfully dependent on costly feedstock from Nigeria; at $40 a barrel, it's the most expensive crude that OPEC has to offer. Gulf lost close to $200 million before taxes on domestic refining and marketing operations alone in the first quarter. "The

Exploration Costs

They're soaring. Phillips Petroleum will spend about $10 million to drill a wildcat well in southeastern Arizona, where the mud-splattered roughneck at left is handling equipment used to hoist and disassemble drill pipe. It will be a year before the well reaches the targeted depth of 20,000 feet—and before Phillips learns whether its gamble has paid off.

Consumer Demand

Long gasoline lines are just a memory in today's buyer's market, as these New Jersey green flags, solicitous service, discount coupons, and price competition make clear. The jump in pump prices has forced conservation, but the trend could change when the economy picks up—or if consumers get used to the new prices.

whole downstream business was under water," says Robert W. Baldwin, president of Gulf's refining and marketing. "We were just a little deeper under water."

A number of savvy Wall Streeters, citing these and other grim forecasts, are skeptical that oil-company stock prices will rebound soon from this summer's lows. William Randol, an analyst with Salomon Brothers, expects the group as a whole to be "dull performers," perhaps through 1982. Morgan Stanley's Barry Good believes that prices may not even have bottomed out. He's also unmoved by a startling statistic: the integrated oil companies are selling at less than 50% of "breakup" value per share, the theoretical price a stockholder would receive if all of a company's assets were liquidated. In today's market, he says, good companies in a host of industries sell far below their liquidation value.

A bull at Paine Webber

While Good and others may be right in their short-term pessimism about oil stocks, others in Wall Street argue persuasively that the investing public has overreacted to the industry's fall from grace. "I haven't been as bullish on the oils since 1974 and 1975," says Bruce Lazier of Paine Webber Mitchell Hutchins. Between 1982 and 1985, Lazier predicts, the integrated companies will increase their earnings per share by at least 15% a year—more than a lot of other sectors of the economy can hope for.

Oilmen see bargains aplenty, both in their own stocks and in those of others. Texaco, Indiana Standard, and Gulf have announced plans to repurchase some of their outstanding shares—up to 5% in Gulf's case. At a recent quote of $39.75, the stock of a much smaller outfit, Pennzoil, looked "too tempting" to Chairman J. Hugh Liedtke. So Pennzoil (1980 sales: $2.5 billion) will buy back up to 2% of its equity. Says Liedtke: "This is the greatest buying opportunity for oil, gas, and mineral stocks that I've seen in years, or may ever see."

Vivid proof that Liedtke's confreres agree with him lies in the feverish bids and counterbids for Conoco by Seagram, Du Pont, and Mobil. Others have mergers in mind, too—either making them or fending them off. They're spurred on by an Administration that doesn't regard bigness as badness. Exactly how far Washington will go in allowing mergers, particularly of the "horizontal" type between companies in the same business, may become clearer in the next few days or weeks. If the Reaganites challenge Mobil's takeover bid for Conoco, for example, they will be drawing the line at mergers involving two major oil companies. If they don't, the money spent this year buying oil and gas reserves through takeovers could run in the tens of billions of dollars—a mind-boggling prospect.

The table on pages 54 and 55 shows why takeovers are so appealing. In today's bear market, it's cheaper to buy reserves on the floor of the New York Stock Exchange than to hunt for them in more daunting terrain. But takeover opportunities haven't diminished the industry's appetite for punching holes in the ground. Indeed, the hydrocarbon hunt thunders onward at breakneck speed—another sign of oilmen's optimism in the face of a glut. The $45 billion that oil companies plan to spend in 1981 on domestic exploration and production is more than double the 1978 level.

In June, over 4,000 drilling rigs were at work in the U.S., a record. Baker International, a leading oil-service company, projects that as many as 5,800 rigs could be "making hole" by 1984. "The growth for our products and services is going ahead as if the glut did not exist," says E. H. "Hubie" Clark Jr., Baker's chairman and president.

What's going on here? Have industry executives contracted a terminal case of oil-patch myopia? Not to hear them tell it. Though takeovers are the cheapest path to reserves right now, they say, they are mere reshufflings of what has already been found. Despite an improved showing, the industry as a whole still isn't finding as much oil and gas in the U.S. as it is pumping. Hence each company's quest for new reserves to supplement whatever can be acquired.

In laying out those growing sums for exploration, oilmen are convinced they

Saudi Arabia

How long the oil glut persists largely depends on when Saudi Arabia—ruled by King Khalid, the man in the middle at right—decides to cut back the flood of oil his country is producing in its effort to gain control of OPEC prices.

see an attractive payoff five years down the road, which is the minimum time it takes to bring a new field into full production. Just how attractive will heavily depend on three imponderables that hold the key to profits in the new, down-to-earth era the industry has entered—the cost of finding new reserves, consumer demand, and Saudi Arabia's ability to influence world oil prices.

"We're in a classic squeeze"

Finding costs are difficult to pin down; they include everything from payments to drilling contractors to the enormous "lease bonuses" the majors regularly plunk down for the right to drill in state and federal offshore waters. Still, most oilmen agree that they have been rising at a blistering rate—at least 20% a year. B. P. "Pete" Huddleston, a thoughtful independent petroleum engineer based in Houston, figures that finding costs now stand in the neighborhood of $15 to $17 per barrel of oil. "Every activity associated with the oil business is overpriced—from drilling mud to petroleum-engineering consultants," he says.

Oil-field inflation shows no signs of subsiding over the near term, even though U.S. crude prices have backed off from their post-decontrol highs by around $3 per barrel. "We're in a classic squeeze," says Rawleigh Warner Jr., chairman of Mobil. James L. Ketelsen, chairman of Tenneco, is even more worried. His company is one of the few whose new discoveries and other reserve additions have replaced production in the past few years. But by the end of 1982, Ketelsen fears, Tenneco may find exploration costs too high to keep up this enviable record.

The picture is not as gloomy as it looks, however, because the supply of oil-field equipment—whose producers have embarked on huge expansion programs—promises to catch up with demand. Baker International's Clark predicts that oil-field inflation will fall to a relatively manageable 10% in a few years.

At the moment, of course, a surplus of crude is sloshing around the world oil markets. Overall, the OPEC countries are pumping about 23 million barrels a day, not much more than 70% of their total capacity.

But most oilmen are betting that they'll have no trouble profitably selling any oil and gas they find. The glut is partly illusory. The oil companies are working off bloated inventories to reduce sharply higher carrying costs, and thus are temporarily reducing perceived demand for crude. Nevertheless, some Wall Street bears are spinning a scenario that includes the surplus as a virtually permanent fixture on the scene. "The glut is here to stay," opines Henry L. Wojtyla, an economist with the brokerage firm of Rosenkrantz Ehrenkrantz Lyon & Ross. Wojtyla believes that as non-OPEC production increases in Mexico, the North Sea, and elsewhere, the demand for OPEC crude could tail off to 16 million barrels a day as early as 1983.

John H. Lichtblau, executive director of the Petroleum Industry Research Foundation, an industry-supported group, meanwhile forecasts that the demand for petroleum products in the U.S., including gasoline, will contract some 10% between 1980 and 1990. From here it is but a short hop to the conclusion that the price of oil will remain flat, in real terms, and could conceivably head straight south for several years.

An audience of oilmen was recently startled by figures from the Houston consulting firm of Groppe Long & Littell; they predicted crude prices of $15 per barrel by 1985 (in constant 1980 dollars). A new study by two Stanford University professors, Henry S. Rowen and John P. Weyant, also sees a possible collapse in oil prices, to as low as $20 a barrel within the next two years (in 1981 dollars). Their thesis holds that consumers will cling to their new conservation ethic—even if oil supplies continue plentiful. The professors calculate that every million barrels a day of excess production in 1982 could result in a $6 to $8 decline in the real world price of crude.

It is not preordained, though, that demand will go on falling. A few analysts see U.S. consumption of petroleum products hitting bottom fairly soon and starting to creep up thereafter by 1% to 2% a year. Conoco has forecast that worldwide demand will increase by 2.1% a year through 1990. But even if demand slowly declines in the industrialized world, as most now expect, prices needn't follow it downward. This is because of Saudi Arabia's great muscle when it comes to influencing prices.

The current world oil surplus, on the order of two million to three million barrels a day, is largely a creation of the Saudis. In an effort to wrest control of prices from OPEC hawks like Kuwait and Libya and to moderate future price increases,

continued

Saudi Arabia has been producing more than ten million barrels a day. It now accounts for 40% of the cartel's production, compared with only 21% in 1972. Sheikh Ahmed Zaki Yamani, the Saudi oil minister, believes that OPEC prices shot up too high after the outbreak of the Iran-Iraq war curtailed exports from those two countries. With its huge reserves, which won't run dry for a half-century, Saudi Arabia has a special interest in keeping prices within reason. Last January, Yamani warned in a speech that if the prices aren't moderated, the industrialized world could be driven into synfuels and other oil substitutes and that demand for Saudi crude could drop to a mere three million barrels a day by the end of the decade.

But just as they can hype production in an effort to pull down world prices, the Saudis can also slash production to prop them up. Walter J. Levy, a noted consultant on petromatters, believes that once the Saudis succeed in unifying OPEC prices at a level closer to their own desiring, they will turn down the spigots and the glut will disappear in short order. Says Levy: "What the sheikhs give, the sheikhs can take away."

Washington

If the Reagan Administration continues to look favorably on mergers, oil stocks could start to sizzle for this reason alone. But Assistant Attorney General William Baxter (below), the antitrust boss, hinted recently that he may stifle big oil's urge to merge. "If they think we're generally soft on mergers," he was quoted as saying, "they're in for a big surprise."

Susan McKenney

How low can the Saudis go?

Just how large a production cut the Saudis might make is an open question, answerable only after Iraq and Iran lay down their arms and repair to the pumping stations. Yet even if those two nations could manage to boost their combined output by two million to three million barrels a day, Saudi Arabia could make offsetting cuts without unduly crimping its audacious development plans. Hisham Nazer, the Saudi planning minister, has said that his country could cut oil production as much as 50%. Some Western observers doubt that the Saudis would ever go that far, and assert that six million barrels a day is the minimum they could live with.

Nobody knows just what price level the Saudis are seeking, and it's always possible that the desert kingdom could fall apart politically at some point or curtail its production in retaliation for U.S. policy toward Israel. But assuming the Saudis do as they say, a reasonable hypothesis is that OPEC prices will average about $34 a barrel early in 1982, compared with a peak price of $41 in 1980. Thereafter, they would probably move in lockstep with the industrial world's inflation rate or a bit faster—at least until another Mideast crisis caused a new supply disruption and a further price spiral.

If the Saudis can bring all this off, they will build a floor not only under world oil prices but also under oil prices within the U.S.—and hence under the profits from domestic production. Meanwhile, U.S. producers have a few cards of their own to play. Big economies remain to be achieved in the downstream end of the business, particularly in refineries. And government policies can help, in ways that promise to improve the bottom line.

The windfall-profits tax, though onerous, will become less so. The levy established three broad tiers of domestic oil—defined according to when and where the oil was discovered, the amount of production per well, and so forth—and taxes the difference between wellhead prices and several so-called base prices at rates that range from 30% to 70%.

The top bracket essentially covers oil discovered more than two years ago, about three-fourths of current U.S. production. Crude found since then, something like 10% of the total, is taxed at a mere 30%. As the mix between old and new oil shifts over time, the typical producer will earn more from production, even if the price at the wellhead stays the same. John Ryan, an analyst with Houston-based Rotan Mosle, predicts the increase will run about 6% to 7% a year. The Reagan Administration is seeking cuts in

The Allures of 16 Big Oil

Company	Oil and gas reserves Barrels per share*	
	Worldwide	U.S.
Exxon	16.6	6.5
Mobil	12.1	4.5
Texaco	15.4	9.2
Standard (Calif.)	8.6	6.4
Gulf	15.1	8.6
Standard (Ind.)	16.9	10.5
Atlantic Richfield	19.9	19.3
Shell USA	11.7	11.2
Conoco	15.5	9.8
Phillips	14.1	7.0
Standard (Ohio)	19.4	19.4
Getty	29.1	22.1
Union	11.1	8.6
Marathon	30.0	16.9
Amerada Hess	14.2	5.2
Cities Service	10.2	9.5

*Gas converted to oil equivalent

	U.S. gas reserves Barrels per share* (Lower 48 states only)	Rate at which U.S. oil and gas discoveries are replacing production	Stock-price range Last 12 months	Recent price	Price-earnings multiple	Stock-market value per barrel of U.S. oil and gas reserves*
	1.7	22%	32⅜-44⅜	$34.75	5	$5.35
	2.4	34%	27¼-44¼	$30.25	5	$6.72
	4.7	25%	33⅛-54⅜	$36.25	4	$3.94
	2.4	42%	35⅛-51¾	$40.00	6	$6.25
	3.9	42%	30⅝-52¾	$36.75	6	$4.27
	4.8	56%	49-99½	$58.00	10	$5.52
	3.1	46%	40¾-74⅜	$48.50	8	$2.51
	3.9	61%	34-65½	$45.25	9	$4.04
	4.1	42%	47½-89⅛	$86.75	11	$8.85
	3.5	18%	34¼-62⅞	$44.25	6	$6.32
	0.2	9%	42⅜-91½	$48.75	6	$2.51
	5.3	22%	59-108¼	$72.25	7	$3.27
	5.5	74%	27⅝-56½	$38.50	10	$4.48
	5.6	30%	44¾-82½	$65.25	13	$3.86
	2.2	15%	26⅝-54¾	$32.25	5	$6.20
	5.9	56%	31¼-62¼	$56.75	13	$5.97

This table shows striking disparities among some widely followed integrated oil companies and in the stock market's assessment of them. A possible reason Atlantic Richfield's U.S. reserves are valued at only $2.51 a barrel (the figure in the last column) is that two-thirds of its gas is in Alaska. It can't be converted to cash until a long pipeline is built. The $8.85 figure for Conoco, of course, is fueled by all the recent merger action. The middle column provides stark evidence that big oil is coming up dry too often; it's not finding enough oil and gas in the U.S. to replace domestic production. The percentage for each company is an average for the past three years and includes only new discoveries and extensions of existing fields. The figures do not include revisions of previous reserve estimates, nor do they take account of additions to reserves through enhanced recovery techniques. The column showing gas reserves in the lower 48 states is important because of the steadily increasing prices allowed by deregulation. The worldwide reserves per share at the extreme left of the table do not include the first four companies' share of Aramco crude-oil reserves, which Saudi Arabia will not disclose.

the windfall levy that would improve those projections somewhat.

And then there is the earnings kicker in the offing from natural gas. Under the timetable set forth in the Natural Gas Policy Act of 1978, wellhead prices will jump 20% annually through 1985. Natural gas now accounts for about one-third of wellhead revenues, and working that number into his projections, Ryan concludes that industry revenues from oil and gas production will climb at about 11% a year—again assuming flat crude prices. Clearly, companies with large gas reserves will benefit the most, particularly those whose reserves are mainly connected to existing pipelines in the lower 48 states.

If crude prices trend downward in the U.S., as they have since last spring, the integrated oil companies could reap a wholly unexpected windfall of another sort, again courtesy of the federal tax laws. Downstream operations are taxed at the corporate rate of 46%, while the top marginal tax rate on crude production verges on 85%, including windfall and severance taxes. Because of this fat spread, according to Bernard J. Picchi of Salomon Brothers, a profit squeeze upstream could be more than offset by gains downstream. A $1-per-barrel drop in U.S. oil prices, Picchi says, could conceivably swell the net income of the 16 integrated oil companies he surveyed by as much as $1.3 billion.

While the aggregate picture of the oils that emerges from all this is more encouraging than is generally recognized, there are enormous disparities among the companies. Says Bill Kieschnick, Atlantic Richfield's president: "It's like asking if you can walk out and drown in a river with an average depth of three feet."

The disparities could affect the future more than the present, as is shown by a close look at four companies—Arco, Texaco, Mobil, and Indiana Standard. Analysts are generally predicting flat or slightly rising earnings for the four in 1981, but after that their fates could vary considerably. Arco's aggressive oil hunt, for example, has put it in a superior position in terms of self-sufficiency. It produces most of its own crude, practically all of which comes from the U.S. Atlantic Richfield has a large share of the production at Alaska's Prudhoe Bay, and early in 1982 will bring onstream the Kuparuk River field to the west. By 1986, gross production there could reach 200,000 barrels a day, of which Arco's share will be roughly 60%. Largely because of Kuparuk and Prudhoe Bay, Kieschnick can make the claim, rare among the majors, that "from what we already have in the 'bank,' we see stable, non-declining oil production for over a decade." Adds William Randol of Salomon Brothers, "It's one of the few companies you can point to with conviction and say it's going to have volume growth."

"A nice little nest egg"

Those volumes should be highly profitable, too, especially the Kuparuk River production. The way Congress wrote the windfall-profits tax, production from this field will escape the levy entirely. Natural gas is more of a question mark for Arco; two-thirds of its gas reserves are locked in Alaska, awaiting financing and construction of a $30-billion pipeline. Still, Kieschnick is happy to have the stuff: "It's a nice little nest egg."

Texaco, by contrast, has a dismal record in finding hydrocarbons. Its U.S. crude reserves fell 7% in 1980, and its domestic reserves of natural gas have declined by 42% over the last three years. Unlike Arco,

continued

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Mobil can't replace production through discoveries alone, says Rawleigh Warner.

though, Texaco has benefited by processing Saudi crude, whose price has generally been $2 to $4 a barrel below the OPEC average. It holds a 28% interest in Aramco, the Arabian American Oil Co. (The other partners: Exxon, Standard Oil of California, and Mobil.) Estimates vary, but the so-called Aramco advantage may well have pumped up Texaco's after-tax downstream earnings by over $350 million in 1980. Unfortunately for Texaco and the other Aramco partners, this advantage could disappear this year if the Saudis can succeed in unifying OPEC's chaotic price structure.

Under prodding by its new chief executive, John McKinley, the company has mounted a serious effort to stem the decline in its U.S. reserves. It has upped its domestic exploration and production budget this year, to about $1.3 billion. But the best Texaco can hope for, says Robert R. McCall, senior vice president for exploration and production in the U.S., is to "diminish the rate of its reserve depletion." McCall's comment explains why the company flirted briefly with Conoco and is widely expected to take a run at another outfit soon.

Mobil has always had reasons to prowl. Traditionally crude-short domestically, it also has a much smaller share in Saudi Arabia's production than the other Aramco partners. In 1979 Mobil won the bidding for General Crude Oil (price: $792 million) and the following year bagged TransOcean Oil ($715 million). Sun Oil edged Mobil for Texas Pacific, the subsidiary sold in 1980 by Seagram, and lately Mobil has been battling with Du Pont and Seagram—the oil seller turned buyer—for control of Conoco. "We can't consistently replace production through discoveries alone at our size," Chairman Rawleigh Warner explains. "That's why you see these attempts."

Unlike Texaco, though, Mobil has had a remarkable hot streak in wildcatting, particularly outside the U.S. The Hibernia field off the coast of Newfoundland ultimately could yield reserves of more than two billion barrels of oil by some accounts, and Mobil's interest there is the largest of any operator's. Elsewhere in the world, the company has scored impressive strikes in the Republic of Cameroon and West Germany, among other places.

Mobil's exploration success abroad is equaled, if not exceeded, in the U.S. by Indiana Standard's record. No other major is as aggressive on the homefront. Standard controls 30 million acres, over twice Gulf's domestic lease acreage, and has regularly drilled more wells than any competitor. Indiana Standard's two most notable coups have been in the Western Overthrust Belt and along the Tuscaloosa Trend in Louisiana (see "How Amoco Finds All That Oil," FORTUNE, September 8, 1980). The company may book enough additional reserves this year to replace production. Moreover, John Swearingen swears that Standard can repeat this performance "on an indefinite basis."

Up until last fall, the market loved the Indiana Standard story: the company's stock price appreciated at an annual rate of 30% between 1975 and 1980. But Standard has since slumped further than almost any other integrated company. Part of the blame for the sell-off falls on losses in downstream operations.

The oils aren't finished

How then to explain the steep dive in Standard's share price—and the flight from big oil in general? It is hard to escape the conclusion that the market has become transfixed with a glut that may soon disappear and a temporary lull in quarterly earnings growth that may shortly end. Indeed, says First Boston's Tom Petrie, "the worst year-to-year comparisons are already behind us."

Despite the prevailing sentiment in the stock market, the game is far from over for the oils. The group as a whole may not gallop off the charts for the time being, at least until the next flare-up in the Middle East. But if an investor has a little patience, picks selectively, and can ignore the growling of the bears, that oil on the floor of the stock exchange may be worth mopping up. ■

Chris Collins

DIRECTORY

The 50 Leading Exporters

Exports are becoming ever more important to the U.S. economy—precisely as their expansion seems ever more difficult. Ten years ago only around 4% of GNP could be attributed to exports; they now account for twice that proportion. But U.S. export growth has been unable to keep pace with foreign competition. During the last decade the American share of the non-Communist world's exports has slumped from 15.4% to 12%, with little hope of improvement in the near future. So far, though, the leading U.S. exporters appear unscathed. The top 50 exporting companies are listed at the right, in a ranking based on the FORTUNE 500 directory of the largest U.S. industrial corporations.

Along with direct exporting to foreign customers, U.S. corporations have traditionally advanced into foreign markets through a worldwide network of subsidiary companies. These subsidiaries include both local manufacturers and outfits marketing products from the U.S. parent. In an effort to give a more representative picture of a company's achievements in foreign trade, this year's FORTUNE list (unlike last year's) takes into account sales through foreign subsidiaries as well as those made directly. One result is the inclusion of 15 industrial giants that export almost exclusively through foreign affiliates—notably General Motors, Ford, and International Business Machines, each of which annually exports well over $1 billion of goods. The 50 leading exporters amassed total sales of some $57 billion in 1980—more than one-quarter of all U.S. merchandise sold abroad.

The stubborn obstacles

While summary figures are clear enough, the statistical details can get slippery. Some companies price their sales to their subsidiaries at cost plus markup, others at market value. In addition, sales to subsidiaries are eliminated from a company's consolidated sales totals, so there is a margin for error in the calculations of exports as a percentage of total sales.

The U.S. needs to expand exports of goods and services to preserve jobs and encourage growth. In a worldwide atmosphere of growing protectionism, the Reagan Administration is trying to shape a trade policy to ease some disincentives facing exporters and to make U.S. exports more competitive in world markets. This effort entails modifying the antibribery law, reducing taxes for Americans stationed abroad, and relaxing the banking and antitrust laws to allow banks to invest in export-trading companies. Possibly several billion dollars could be added to the country's export revenues as a result. But many experts feel that breaking down those barriers is not enough to offset other obstacles facing the American exporter—above all, the rising strength of the dollar on world currency markets.

—CLAIRE MAKIN GREEN

THE 50 LEADING EXPORTERS

RANK '80	RANK '79	COMPANY	PRODUCTS	EXPORTS ($000)	FORTUNE 500 SALES ($000)	FORTUNE 500 RANK	EXPORTS AS PERCENT OF SALES %	EXPORTS AS PERCENT OF SALES RANK
1	1	**Boeing** (Seattle)	Aircraft	5,503,800	9,426,200	30	58.39	1
2	•	**General Motors** (Detroit)	Automotive vehicles and parts, locomotives	5,287,100	57,728,500	3	9.16	38
3	2	**General Electric** (Fairfield, Conn.)	Generating equipment, aircraft engines	4,265,000	24,959,000	10	17.09	20
4	•	**Ford Motor** (Dearborn, Mich.)	Automotive vehicles and parts	3,453,000	37,085,500	6	9.31	37
5	3	**Caterpillar Tractor** (Peoria, Ill.)	Construction equipment, engines	3,094,000	8,597,800	33	35.99	3
6	5	**E.I. du Pont de Nemours** (Wilmington, Del.)	Chemicals, fibers, plastics	2,175,000	13,652,000	15	15.93	23
7	6	**United Technologies** (Hartford)	Aircraft engines, helicopters	2,142,593	12,323,994	21	17.39	18
8	4	**McDonnell Douglas** (St. Louis)	Aircraft	2,065,800	6,066,300	53	34.05	4
9	•	**International Business Machines** (Armonk, N.Y.)	Information-handling systems, equipment, and parts	1,615,000	26,213,000	8	6.16	44
10	8	**Lockheed** (Burbank, Calif.)	Aircraft and related support services	1,358,000	5,395,700	61	25.17	8
11	•	**Eastman Kodak** (Rochester, N.Y.)	Photographic equipment and supplies	1,357,029	9,734,303	29	13.94	27
12	12	**Union Carbide** (New York)	Chemicals, plastics	1,240,000	9,994,000	27	12.41	31
13	9	**Westinghouse Electric** (Pittsburgh)	Generating equipment, defense systems	1,192,000	8,514,300	34	14.00	26
14	7	**Weyerhaeuser** (Tacoma, Wash.)	Pulp, logs, lumber, wood products	1,140,000	4,535,814	83	25.13	9
15	10	**Raytheon** (Lexington, Mass.)	Electronic equipment	1,042,000	5,002,088	69	20.83	13
16	25	**Monsanto** (St. Louis)	Herbicides, textile fibers, specialty chemicals	1,026,400	6,573,600	48	15.61	24
17	•	**Dow Chemical** (Midland, Mich.)	Chemicals, plastics, magnesium metal	909,000	10,626,000	25	8.55	39
18	23	**International Harvester** (Chicago)	Construction and farm equipment, trucks	888,000	6,311,804	49	14.07	25
19	•	**Hewlett-Packard** (Palo Alto, Calif.)	Electronic equipment	831,000	3,099,000	120	26.82	6
20	13	**Archer-Daniels-Midland** (Decatur, Ill.)	Soybean meal and oil, wheat, corn	808,941	2,802,011	139	28.87	5
21	14	**Signal Companies** (La Jolla, Calif.)	Trucks, engines, chemicals	803,800	4,285,300	85	18.76	15
22	24	**Dresser Industries** (Dallas)	Oil-field and industrial equipment	703,700	4,016,300	93	17.52	16
23	•	**Ingersoll-Rand** (Woodcliff Lake, N.J.)	Drills, compressors, pumps, bearings, tools	702,600	2,970,960	129	23.65	10
24	16	**Philip Morris** (New York)	Tobacco products	702,400	7,328,300	45	9.58	35
25	20	**Deere** (Moline, Ill.)	Farm equipment	688,000	5,469,825	60	12.58	30
26	•	**Mobil** (New York)	Lubricating oils	683,000	59,510,000	2	1.15	48
27	18	**Kaiser Aluminum & Chemical** (Oakland, Calif.)	Aluminum	676,300	3,222,100	114	20.99	12
28	17	**Occidental Petroleum** (Los Angeles)	Agricultural chemical products, coal	651,000	12,476,125	20	5.22	46
29	19	**Textron** (Providence)	Helicopters, machine tools, metal products	636,000	3,637,500	102	17.48	17
30	11	**Northrop** (Los Angeles)	Aircraft and related support services	614,600	1,655,400	219	37.13	2
31	•	**Exxon** (New York)	Petroleum and chemicals	593,000	103,142,834	1	.57	50
32	•	**Aluminum Co. of America** (Pittsburgh)	Aluminum	588,900	5,147,600	63	11.44	34
33	33	**Celanese** (New York)	Fibers, chemicals	576,000	3,348,000	107	17.20	19
34	22	**FMC** (Chicago)	Industrial and farm equipment	558,517	3,482,183	103	16.04	22
35	15	**Rockwell International** (Pittsburgh)	Electronic, automotive, and industrial equipment	543,000	6,906,500	46	7.86	41
36	21	**R.J. Reynolds Industries** (Winston-Salem, N.C.)	Tobacco products	535,300	8,449,000	35	6.34	43
37	43	**International Minerals & Chemical** (Northbrook, Ill.)	Potash, phosphate, industrial minerals	463,700	1,789,600	201	25.91	7
38	•	**Digital Equipment** (Maynard, Mass.)	Computer systems and equipment	453,814	2,368,045	162	19.16	14
39	•	**Sperry** (New York)	Computer systems and equipment	453,213	4,785,425	77	9.47	36
40	28	**Williams Companies** (Tulsa)	Phosphate products, fertilizer	444,000	2,072,686	181	21.42	11
41	•	**NCR** (Dayton, Ohio)	Mainframe computers and terminal systems	426,621	3,322,370	108	12.84	29
42	26	**American Motors** (Southfield, Mich.)	Automotive vehicles and parts	421,579	2,552,587	155	16.52	21
43	31	**International Paper** (New York)	Pulp and paper products	411,000	5,042,900	67	8.15	40
44	•	**Phillips Petroleum** (Bartlesville, Okla.)	Petrochemicals, natural gas	374,000	13,376,563	16	2.80	47
45	47	**Emerson Electric** (St. Louis)	Electronic components	371,783	3,066,841	124	12.12	33
46	29	**Allied Chemical** (Morristown, N.J.)	Fibers, plastics, chemicals	369,000	5,519,000	59	6.69	42
47	•	**Control Data** (Minneapolis)	Computers and peripheral equipment	361,900	2,765,609	141	13.09	28
48	•	**Minnesota Mining & Manufacturing** (St. Paul)	Industrial, health-care, graphics, electronics products	361,000	6,079,540	52	5.94	45
49	•	**Standard Oil of California** (San Francisco)	Chemicals, fuel and gas oils	359,000	40,479,000	5	.89	49
50	•	**AMAX** (Greenwich, Conn.)	Molybdenum, nickel, and phosphate products	357,330	2,949,170	131	12.12	32
		TOTALS		**57,277,720**	**599,858,168**			

• Not on last year's list.

Heinrich Ulrich to be joint *Sprecher*. The arrangement, though harmonious, ended in 1970 when Klasen became president of the Bundesbank, West Germany's central bank. All three of these postwar *Sprecher* still contribute to the bank's tradition of continuity. Abs is honorary chairman and Ulrich is chairman of the supervisory board; Klasen, now retired from the Bundesbank, is a member of the board.

Predictions abounded in 1976 that the Christians-Guth brother act would be short-lived. The election had been a cop-out of sorts, because the two were considered equally well qualified and neither would stay on under the other. But both men recognized from the start that they had to stand together or the board would split into factions. Says Christians, "We decided never to go into the boardroom divided on any issue. If we were not initially in full agreement, we sat down and talked until we were."

A changing of the guard

The Eighties will see the third postwar changing of the guard at Deutsche Bank, with Guth reaching retirement age in 1984 and Christians three years later. The succession should cause few problems. The average age of the bank's present executive board is in the low 50s and three of the members are in their 40s. Aspirants to the post of *Sprecher* are already beavering away in hopes of establishing that edge which makes the elections, in the words of Franz Ulrich, "simply the legitimation of an existing situation."

The question will be—one spokesman or two? The success of the present team has lent renewed strength to arguments that continuing a managerial duo at the top has practical advantages—especially as the bank expands in the U.S. and elsewhere abroad. With bankerly charity, Christians notes: "When I see the load that chief executives of banks our size have to carry, I wonder how they can do it alone." Guth adds, "And none of them can be in two places at once." F

The U.S. Pushovers Push Back

A voracious pack of foreign banks has invaded the American market in recent years, offering blue-chip corporations a bonanza of credit and giving U.S. bankers a bad case of nerves. Bank of Tokyo has booked more commercial and industrial loans in this country than any other foreign institution—$2.28 billion as of the end of 1980. By contrast, Deutsche Bank, with a mere $228 million, is a distant also-ran so far. In all, the ten largest foreign lenders have over $17 billion of U.S. business loans tucked in their portfolios—more than the domestic commercial-loan business of Citibank, Chase Manhattan, or any other single American giant.

Some foreign banks have been on U.S. shores for decades, quietly serving clients from their home countries; the Hongkong & Shanghai Banking Corp. set up shop in San Francisco in 1875. In recent years, however, many foreign banks have turned to the U.S. market as a new source of growth. Of the commercial and industrial loans booked in the U.S., the share handled by foreign banks more than doubled from 6% at the end of 1972, when the Federal Reserve began compiling the figures, to 14.3% in June—and much more in money centers like New York.

These figures include loans made by the foreign banks' U.S. agencies and branches, but not by American banks controlled by foreigners—which would make the foreign share even larger. Hongkong & Shanghai owns 51% of Marine Midland, the 15th-largest U.S. commercial bank, and six European institutions own European American Bancorp (No. 27 in the U.S.). Midland Bank of Britain is taking over Crocker National (No. 13). If loans booked by all foreign-owned U.S. banks were included, the foreign share of the New York business-loan market would have reached 41% at the end of last year.

Research associate: Ford S. Worthy

The most aggressive European and Japanese banks have dotted the countryside with representative offices and branches. Over the past decade, foreign banks have opened more than 200 offices in financial hubs such as New York and Houston. The account officers there are under pressure to get loans on the books, so the expansion has added angst to the already fiercely competitive market. Loan officers scour the back roads of corporate America, knocking on treasurers' doors to solicit any business they can scrounge.

Balance-sheet puffers

Wresting a corporation from its long-standing relationship with a domestic bank is easier said than done, however, so foreign bankers do battle with the ultimate weapon—bargain-basement loans. Japanese and French bankers, known to be among the most aggressive, make 30-day "money-market loans" priced as low as an eighth of a percentage point above their cost of funds (with no "compensating balance" required from the borrower). "They're just puffing up their balance sheets with those kinds of unprofitable loans," says one Canadian banker.

Even before spreads shrank as much as they have today, well-established, conservative foreign banks—the Canadians among them—introduced fixed-rate loans based on the London Interbank Offered Rate (LIBOR). Several years ago, LIBOR ran as high as the U.S. prime rate or higher. But lately, LIBOR has sunk as much as three percentage points below the prime. The low LIBOR

reflects the large quantity of funds flowing into the Eurodollar market and the economies of scale of handling huge deposits. LIBOR-based loans—plus the ability of corporations to raise money cheaply in the commercial-paper market—have pressured U.S. banks to trim their own lending rates below prime.

Why have the foreigners been so anxious to compete for low-profit business? Many say they are simply following their local customers abroad, just as U.S. banks followed American multinationals when they expanded overseas 20 years ago. Having made the decision to enter the U.S., the banks have been willing to forgo short-term earnings to stake out a piece of the world's largest, most dynamic commercial-loan market. A lot of foreign bankers view the U.S. as a wide-open frontier for banks facing slow growth at home. The Germans, British, and Japanese see their native markets as "overbanked," while local credit controls have also encouraged the French and British to look for business elsewhere. Bankers from developing nations like Brazil want to lessen their risks by diversifying beyond local borrowers.

Irresistible advantages

Until recently, foreign banks had competitive advantages that made the move into the U.S. irresistible. Exempt from many restrictions on U.S. banks, they could branch across state lines and buy up domestic banks that their American competitors were forbidden to touch. Foreign-bank branches were not required to set aside a portion of their deposits in non-interest-bearing reserves as U.S. banks are. And their home-country regulators allowed them to support more loans on a smaller capital base than their U.S. counterparts. These advantages lowered the foreign banks' costs, giving them a competitive edge.

Before long, American bankers pressured Congress into equalizing the rules for all contestants. The International Banking Act of 1978 limited the foreign banks' interstate expansion and imposed reserve requirements that will be fully phased in next year. Foreign bankers now feel the competition has been more than equalized. "If the purpose of the law was to make our cost of funds higher," says a top Japanese banker, "then the purpose was certainly attained."

Foreign banks in the U.S. raise about one-third of their funds in the Eurocurrency markets and the rest here. They usually pay more for funds in the U.S. than domestic banks do because they have fewer retail branches to provide cheap money from low-interest checking accounts. They raise funds mainly by selling certificates of deposit and commercial paper. Serge Bellanger, executive vice president of the New York branch of Crédit Industriel et Commercial, a big French bank, says foreigners generally have to pay a premium for this money. "Domestic banks have the advantage," he says, "because they are well known to the U.S. money market, while many foreign banks aren't." By the time the new reserve requirements are fully phased in, Bellanger estimates, foreign banks will have to set aside roughly $1.8 billion in non-interest-bearing accounts; at today's interest rates that would cost the banks more than $300 million in potential earnings.

Time to slow down

Now the American banks are beginning to fend off the competition. On major loans, they are frequently offering the "LIBOR option"—letting the customer pick a LIBOR-based rate rather than the prime. They are getting adept at foreign-exchange dealing and international-trade finance, where foreign bankers held an edge. Plenty of foreigners admit that the Americans they once regarded as pushovers are getting tough.

So with new competition and the loss of their cost advantage, the foreign bankers see their market shares leveling off or dipping a bit. "We need to slow down," says Bellanger. He thinks foreign banks will have to try to widen their loan spreads. Wilfried Guth, co-chief executive of Deutsche Bank, says the banks need a full percentage-point margin. If the players in the U.S. market hope to reach that, they'll all have to curb their lending appetite for quite a while. —EDWARD MEADOWS

The Top Ten Foreign Lenders

LOANS TO BUSINESS IN THE U.S.

	(billion)
Bank of Tokyo	$2.277
Dai-Ichi Kangyo Bank	$2.019
Mitsui Bank	$1.866
Fuji Bank	$1.784
Bank of Montreal	$1.762
Canadian Imperial Bank of Commerce	$1.721
Royal Bank of Canada	$1.496
Swiss Bank Corp.	$1.456
Sumitomo Bank	$1.438
Mitsubishi Bank	$1.375

The Japanese handily lead this ranking of foreign banks lending to business in the U.S. The figures include all business loans booked in the U.S. by foreign-bank branches and agencies as of December 31, 1980. The Japanese lead is exaggerated by some peculiarities of international banking. While the Japanese record virtually all loans to borrowers in the U.S. on the books of their American operations, other foreign banks often book loans in Caribbean tax havens, which means those loans don't show up in U.S. figures. The data were supplied by the *American Banker*.